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August 15, 2003

Ms. Marlene H. Dortch  
Federal Communications Commission  
Office of the Secretary  
445 12th Street, SW  
Washington, DC 20554

RE: *Ex Parte* Presentations in CS Docket No. 97-80 (Implementation of the Section 304 of the Telecommunications Act of 1996: Commercial availability of Navigation Devices); PP Docket No. 00-67 (Compatibility between Cable Systems and Consumer Electronics Equipment); and MB Docket No. 02-230 (Digital Broadcast Copy Protection)

Dear Ms. Dortch:

This is to notify the office of the Secretary that on August 14, 2003, Jack Valenti and Fritz Attaway of the Motion Picture Association of America, accompanied by Paul Heimbach and Anne Lucy of Viacom Inc., Richard Bates and Troy Dow of The Walt Disney Company, Linda Bloss-Baum of Vivendi Universal Entertainment, and Rick Lane of News Corporation held an *ex parte* meeting with FCC Commissioner Johnathan Adelstein. In addition, the above mentioned, Heimbach, Lucey, Bates, Dow, Bloss-Baum, and Lane held an *ex parte* meeting with Anthony Dale Interim Media Advisor for FCC Commissioner Kevin Martin on the same day.

The meetings covered material submitted to the FCC in the Joint Comments of the Motion Picture Association of America, et al. on March 28, 2003, and Reply Comments on April 28, 2003, in CS Docket No. 97-80 and PP Docket No. 00-67, and in Joint Comments on December 6, 2002, and Reply Comments on February 20, 2003, in MB Docket No. 02-230.

The *ex parte* presentations focused on the following points:

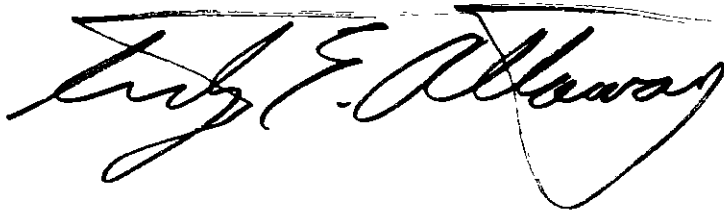
- Adoption of a "Plug & Play" regulatory scheme should be based on multi-industry negotiations where all interested parties are provided an opportunity to participate.
- Subpart W is not necessary to achieve interoperability of cable interface devices.
- Subpart W issues should be resolved by marketplace negotiations among content owners, distributors and ultimately users.
- Subpart W forecloses new business models by imposing regulated, mandated content usage rules.

- Content providers and other interested parties should have an opportunity to participate in an open process to select new, protected outputs and de-certify previously protected outputs that have been compromised.
- Subpart W perpetuates the analog hole and discourages a complete transition from analog to digital.
- The same product cycle concern that supports prompt action on Plug & Play requires prompt action on Broadcast Flag. The first generation of Plug & Play receivers should not be rolled out without the broadcast flag technology.

In addition, the attached document, "'Napster-ization' Threat of Video Content Growing," was handed out to some of the meeting participants.

In accordance with Section 1.1206 of the Federal Communications Commission rules, this original and one copy are provided to your office. A copy of this notice is being delivered to the parties mentioned above.

Sincerely,

A handwritten signature in black ink, appearing to read "Eric F. Allaway". The signature is fluid and cursive, with a large, sweeping loop at the end.



**Precursor Group**

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AUG 25 2003

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David R. Hoover  
Rudy L. Baca  
August 7, 2003

## "Napster-ization" Threat of Video Content Growing

(Part III in a Content Digitization Series)

**Summary:** Precursor cautions investors not to underestimate the growing impact of digital video piracy and its threat to content providers such as VIA, DIS, and FOX. Technical barriers to obtaining video content will likely continue to lessen over time. Improvements in copying, compression and storage, the growth of broadband, and the increased ability to transfer content between devices will give consumers more control over how, when, and where video content will be viewed. Whether consumers do so lawfully or not depends in part on how quickly and successfully content owners react. Precursor believes Hollywood has roughly a two-year window to make substantial progress in protecting its content and offering compelling alternatives to illegal file-sharing. Otherwise, the industry's ability to fully monetize segments of its video release chain will likely be crippled by growing piracy.

**Theft of Video Content Shadowing Music.** Illegal swapping of video content still pales in comparison to audio files. However, Precursor believes the threats to Hollywood will ramp up, as finding, downloading, and displaying content become easier and more widespread. Some good proxies of video content theft already exist. The sale of blank media is becoming substantial. 16 million blank DVDs were shipped in the first five months of '03, perfect for burning large video files. Over 70m copies of DivX 5.0—compression software key to efficiently storing and distributing content—have been downloaded. Finally, the Motion Picture Association of America (MPAA) estimates over 600,000 video files are traded daily through Internet channels (P2P, IRC).

**The Hassle of Copying Video Diminishing.** (A) **Finding Content: More Available on P2P.** A dozen widely utilized P2P networks, along with Internet Relay Chat and File Transfer Protocol, provide consumers with many file-sharing opportunities. With an average of 6-7m people connected to P2P networks daily, the ability to find any type of content illegally is much greater than on industry pay sites. The pay services must negotiate licensing agreements for online distribution of content, a time-intensive task that delays and sometimes excludes the availability of content. Sources of illegally traded video include stolen master studio prints, video camera theater tapings, recordings of broadcast television, and compressed copies of DVDs. Though quality varies much of it is passable, including television content, which is mostly stripped of advertising. (B) **Downloading Content: Broadband Drives P2P.** Downloading video is difficult without high-speed access but the number of broadband users and throughput capabilities are more likely to increase. The

average compounded growth rate for U.S. broadband adoption for the last three years is over 100%. Roughly 19m U.S. households subscribe to a broadband service. Conservatively, high-speed access lines could grow 20%-25% annually for the next two years. Innovative applications that improve the distribution of content, especially large media files, are freely available. eDonkey and BitTorrent efficiently split files into smaller parts, making those pieces immediately available to other users through balanced uploading and downloading. (C) **Displaying Content: Easier to View and Store.** The ability to easily transfer downloaded video content to other devices for viewing will enhance the utility of P2P. 802.11g and Ultra-Wideband, with theoretical bandwidth speeds of 54 Mbps and 100 Mbps respectively, will enable better streaming of large files from the PC to TV. Additionally, the impact of increased storage in digital video recorders, DVD players, and PCs will likely erode the aftermarket value of Hollywood's television and movie content, as consumers save more video files. ~60% yearly increases in disk storage capacity and ~40% yearly declines in cost per megabyte of storage price feed this trend.

**Release Windows Open to Business Model Threat.** Hollywood's business model is based on a series of theatrical release windows, timed to maximize revenue. Films typically transition from theaters to home video, pay-per-view, video-on-demand, network/cable television, and syndicated television—each roughly every six months. As consumers gain access to pirated content, Hollywood is losing its tight grip on the timing and control of these windows. In defense, studios are shrinking the windows, but the monetization of down-market opportunities is largely based on the success of content in earlier windows.

**Illegal File-Swapping Defenses.** Studios are facing an uphill battle in thwarting video piracy. The effectiveness of their defenses will be gauged in upcoming Precursor Research. (A) **Paid Content.** Studios are offering subscription and one-off sales of movies, but with limited viewing periods. (B) **Tech Solutions.** (1) Rollout of the Broadcast Flag, with its questionable ability to completely stop illegal distribution of TV content, will likely be lengthy and complex. (2) Studios are "spoofing" (uploading bogus files) and "sniffing" (identifying users by IP address) to thwart illegal file sharing, but P2P is fighting back with file-sharing upgrades that preview content during downloads and anonymizes IP addresses. (C) **Education and Litigation.** Precursor doubts industry can substantially slow digital theft just through educational campaigns and subpoenas. \* \* \* \* \*

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# Digitization Undermines Content Value Model

## Early Evidence Suggests Video Copying Is Shadowing Audio Piracy...

	Video	Audio*
<i>Files illegally downloaded</i>	18 million + (monthly)	2.6 billion (monthly)
<i>Blank media shipped</i>	16 million DVD-R (Jan-May '03)	3.6 billion CD-R (-'02)

\* Primarily audio files

## ...AND Hurdles to Widespread Video Copying Diminish As It Gets Easier to...

### Find Content

- Over a dozen widely-used P2P file sharing applications available with 6-7m users daily
- 300k daily downloads of KaZaa software
- 70m+ downloads of DivX DVD compression software

### Capture Content

- 2Q03 combined cable & DSL residential broadband lines of 18.5m, conservative estimate over 25m lines in 2 years
- At 700 kbps it takes 15 hours to download a high quality uncompressed DVD movie, but only 2 hours to download a typical compressed movie, and ~30 minutes for TV shows
- ~60% yearly increase in disk storage capacity and ~40% yearly decline in cost per megabyte of storage

### Display Content

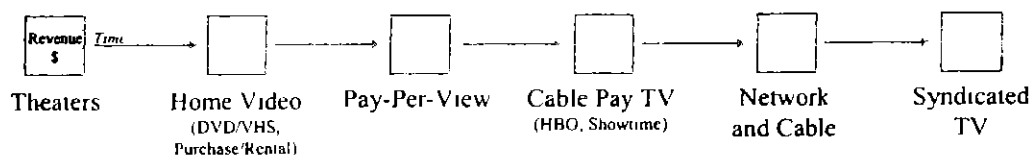
- Wireless home networking solutions geared toward video introduced this year
  - 802.11g wireless networking (WiFi) standard guarantees decent video streaming capacity of up to 54 Mbps
  - Ultra-Wideband is an ideal solution for video distribution at short ranges, with streaming data rates of 100 Mbps

## ...Compressing the Ability to Fully Monetize Content by Shortening Release Windows.

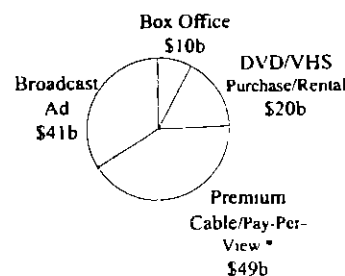
### The "Release Window" Is Dependent on

- Controlling timing of content release
- Offering differentiated viewing windows
- Generating monetary success at each window

Leading to the maximization of revenue over an extended period of time



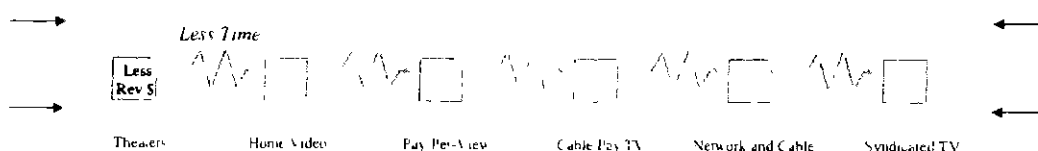
### Ultimately Threatening Content Driven Revenues



### But "Release Window" Is Threatened As Consumers

- Gain earlier access to content through piracy
- Store content for extended and multiple viewings
- Redistribute content through copying or Internet

Pressuring revenue as the size and timing of each window is compressed



**\$120b**

Total Content Driven Revenues

\* Includes subscription/ad revenue